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D.H. HOWDEN & CO. LIMITED

1976 REPORT TO SHAREHOLDERS

HOWDEN

THE FIRST 75 YEARS

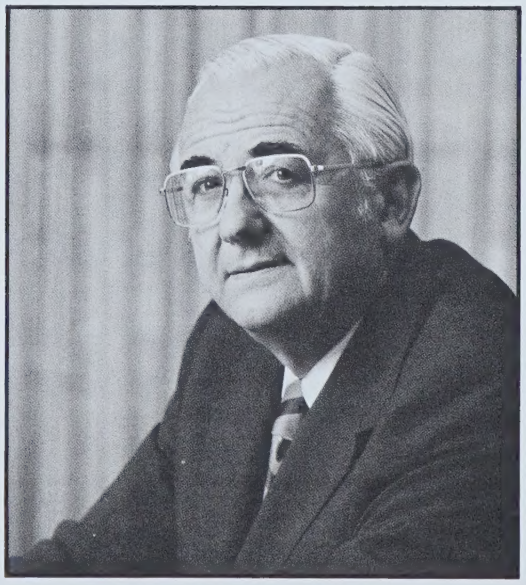
D.H.HOWDEN & CO. LIMITED

1976 REPORT TO SHAREHOLDERS

TO OUR SHAREHOLDERS

This year's Annual Report has as its theme our 75th Anniversary, in contrast to last year's Report which provided an indepth study of Company systems and operations. In a sincere way the Report is dedicated to past and present employees of D.H. Howden & Co. Limited who did and are doing so much to build the Company from its meagre beginning to its present size.

Highlights	**1976**	1975
Gross Sales - increase 18%	**$60,276,244**	$51,028,667
Net income	**902,782**	918,958
Per Common Share	**1.59**	1.62
Inventories	**7,919,376**	6,164,665
Working Capital	**8,956,939**	7,378,251
Ratio of current assets to current liabilities	**2.36:1**	2.07:1
Shareholders' equity per Common share	**10.45**	9.16
Return on net worth	**16.13%**	19.07%



WE report record sales in 1976. Sales rose 18% to $60,300,000 and resulted in net earnings of $902,782, a 2% decrease from 1975. Net profit return on Shareholders' Equity was 16% compared to 19% in 1975. Earning per share was $1.59.

We fell short of our projected profit of $2.00 per share, for the following main reasons:

1. Our 1976 physical inventory was below book inventory in the amount of 20¢ per share. This was unexpected. Customarily the reverse is the case, with actual inventory exceeding book because of inflationary profit on inventory. In the past this has compensated for normal stock wastage factors, such as loss on defective merchandise, shipping errors, etc. However, investigation reveals that in 1976, with the lessening rate of inflation, this full compensation condition no longer existed. In response, we have revised certain of our dealer contracts and policies for better control of wastage factors.

2. We experienced an unsatisfactory last quarter of the year, a period in which sales and gross margins were below budget figures. This was particularly so in the Electrical Division, where volume was low and competition extreme. At the same time, the hardware consumer became more selective in Christmas purchasing, concentrating on promotionally priced merchandise, possibly a reflection of the effect of AIB controls on income.

3. Costs mounted in energy related areas, in transportation and in short term borrowing. Many of these costs we were unable to pass along owing to contractual relations with dealers. We have revised such dealer contracts, effective January 1st, 1977.

4. We experienced higher than expected marketing cost in Western Canada. Now that a broader customer base exists, we expect these expenses to drop to more normal levels.

5. During the last quarter we completed the new White Oaks case goods warehouse, which increases our warehouse capacity to 300,000 square feet, all of it needed to service our expanding dealer organization. During November and December inventory was rearranged within this new facility, creating additional one-time costs.

6. During 1976 the rapid rate of inflation on hardware products declined substantially. In general it can be said that the rapid price increases of the past few years tended through inflationary inventory profit to mask operating inefficiencies, and this has its effect on a business such as ours, which sets as its goal high-yield performance. In 1977 we must exert great care on cost controls.

In advising the Shareholders on fourth quarter results, I do not wish to convey any pessimism as to the future; rather the contrary is the case. The Hardware Dealer Division and the Building Supply Division completed a year of record sales and commendable profits. The number of Pro franchised stores now stands at 290. This number in itself does not explain the degree of work and effort expended in 1976 in modernizing and expanding stores to improve their competitive position. The development of stores in Quebec and the Atlantic Provinces also continued to meet projections. An economic dealer base in British Columbia now exists.

Our 1977 budgets call for continuing growth, not only from existing customers, but from new stores joining our systems. The demand for "do-it-yourself" merchandise, the backbone of our business, continues to remain strong and we look to 1977 with confidence.

The Electrical Supply Division continued to experience problems in generating profit. The Division was able to maintain sales volume, but in doing so, gross margins declined. The cost reduction programs instituted early in 1976 proved insufficient to cover inflationary cost increases. Further changes must be made in 1977 to reduce costs in face of lagging demand.

Computer Horizons (Canada) Limited, our joint venture with Management Horizons Inc. of Columbus, Ohio, continues to grow both in system strength and in knowledge. The business earned a profit in 1976 and expects a profitable operation in 1977.

You will note from the financial statements that we completed the sale of a $4,000,000 debenture to a major lending institution. These new long term funds will improve our working capital ratio, and provide the basis for further expansion. The interest rate is favorable to our long term borrowing cost.

In reporting the results of 1976 on behalf of the Board of Directors, I express appreciation and thanks to our Staff for their dedication and efforts. As a result of their industry and resolution, distribution under the Employee Profit Sharing Program amounted to 7¢ per share.

We thank our customers for their continued patronage. We also thank our suppliers for their support. The future requires that we must continually work closer together if we are to improve our supply service to our customers.

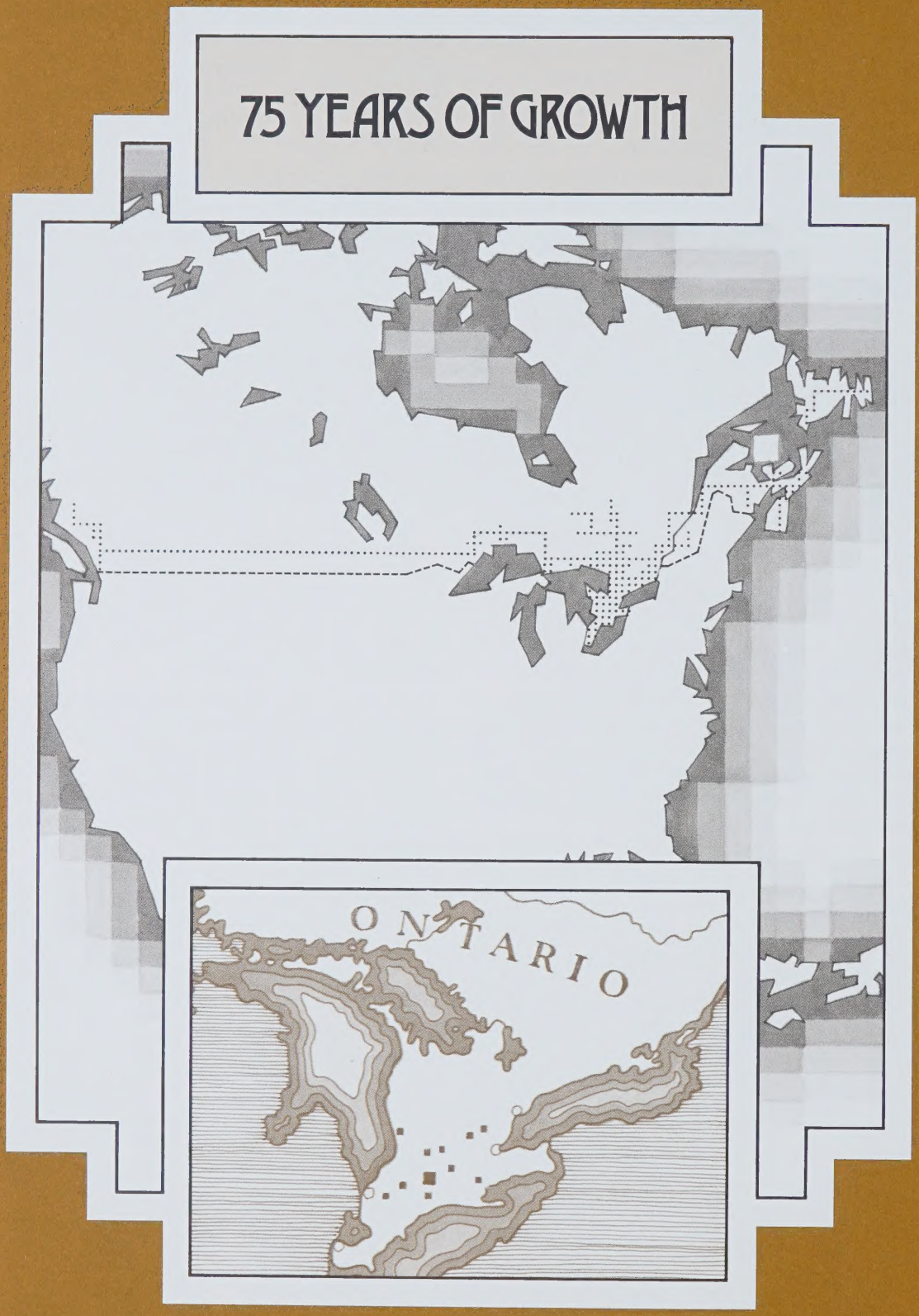
We thank too our Shareholders for their support and are pleased that during 1976 we were able to increase the dividend to 30¢ per share.

On behalf of the Board.



D. H. M. Stewart,
President

75 YEARS OF GROWTH



IN the days before Canada became a nation, Watford, Ontario was a flourishing village.

By the time Confederation was a fact, the village had more than earned the status of "town". When a Strathroy newspaper asked why people called Watford a town, the prompt reply was "We call it that simply because it is not a city". Why not indeed – at that time it was the principal stop between Toronto and Chicago on the main line of the Grand Trunk Railway.

It was a burgeoning community in the latter part of the century, surrounded by fertile farmland, about 25 miles east of the oil and gas fields of Petrolia, enjoying excellent road and railroad connections, beginning to attract industry, and by 1890, proud to boast its own, new and regrettably short-lived bank.

Obviously this was just the place for an aggressive hardware merchant. At age 19, David Hartford Howden, a native of Watford, sensed the opportunity and grasped it. The youngest of a family of seven, the youthful entrepreneur set up shop on Main Street. The store grew faster than the community. Eighteen years later, in 1893, its owner surveyed with satisfaction the capital those years had acquired for him, assessed the more challenging horizons that lay beyond, disposed of his store and set off for a similarly thriving community, London, Ontario.

In 1901, together with partners Lyle Johnston, James Brown, and John Givins, Mr. Howden commenced a new hardware business, but this time as a wholesaler. The scope of the partners' operations quickly spread throughout all of Western Ontario, the dealers being serviced from a site at the corner of York and Richmond Streets in London.

The partnership flourished. In 1904 the London wholesale hardware company of John Bowman and Co. Ltd. failed, and the partners purchased the assets. This was a great forward boost, and in 1907 a limited company was formed. Also in 1907 a new warehouse was built at 200 York Street. It was used until 1960, when it was replaced by the present Southdale Road distribution centre.

David Howden died in 1918 and was succeeded as President by his son, Norman R. Howden. During his administration three other hardware companies were purchased, including the firm of H. S. Howland Sons & Co. Limited, which was the major Central Ontario hardware distributor of that period. Howden then consolidated its Central and Eastern Ontario business into a warehouse at 1 - 3 Church Street, Toronto. It was used continuously until its sale in the late 1960s.

On his death in 1937, Mrs. Lydia Howden succeeded her husband as President, and held office until 1969. At this time Howden went "public" and David Howden Stewart, Managing Director and grandson of David Hartford Howden, became President.

Under his leadership as Managing Director the Company had entered the wholesale electrical business, creating Howden Electrical Supply as a Division of the Company. This Division is now one of the leading electrical distributors in Western Ontario.

The late 1940s and 1950s were difficult years for distributors generally, most of whom operated without a clear sales policy. Taking the initiative, Howden changed course in 1960 and readjusted its targets and purpose. Aided by new facilities, and new franchising and merchandising policies, sales expanded dramatically.

In 1964 Howden, along with 7 other hardware distribution companies, formed Pro Hardware (Canada) Limited, which since has fostered a Canada-wide chain of over 500 franchised retail hardware outlets.

In 1965 Howden incorporated Span-Canada Electric Limited, a corporation which gives its 17 member electrical distribution companies, strategically situated across Canada, advantages of greater purchasing power and earning capacity.

In 1970 Howden and Management Horizons Data Systems Inc. of Columbus, Ohio, through a joint venture, created Computer Horizons (Canada) Limited. This Company markets Management Horizons' computer systems to Canadian distributors of hardware, electrical, plumbing, drug and food products. As its business continues to grow, it provides significant income to the corporation.

At the present time there are 436 employees on Howden payrolls working out of facilities at Southdale Road, and Horton Street in London, and from Electric Division branches in Sarnia and Kitchener. Our customers, while mainly in Ontario, are in excess of 2,000 and range from the Atlantic Provinces to British Columbia.

That those elements of service and value first introduced to bustling Watford now have currency from St. John's, Newfoundland to Victoria, B.C. would surely be pleasing to David Hartford Howden; and no less so to those employees who have served and continue to serve with integrity under the Howden banner. The parade of names through the first half of the century, well and warmly known throughout the industry, is extensive – Rae, Craig, Cryderman, Brown, Thorn, King and so many others.

OPERATIONS REVIEW





IN those early years following 1901, the Howden owners and partners pursued a unique policy: to carry a well-planned inventory; to be a total source of hardware to dealers; and to ship every dealer's order the day it was received. Howden was known throughout the trade as "the quick shippers" and this became the Company's slogan.

With the passage of the years, the philosophy has changed only slightly, but the techniques frequently display a startling break with the past.

Revenues today are generated from three major functions:

a) The distribution of hardware, shelter, leisure and entertainment products to retailers in our 290 franchised Pro Hardware retail stores (Hardware Division), 700 retail Building Supply accounts (Building Supply Division), and 300 Sporting Goods stores (Sporting Goods Division).

b) The supply of advertising and merchandising services and data processing systems to all the above retailers and other distributors.

c) The distribution of electrical construction materials to approximately 1,000 contractors and industrial firms in Western Ontario.

The facilities which host these functions are:

1. A Head Office complex located at 635 Southdale Road, London, Ontario. This is comprised of 240,000 square feet of warehouse and 20,000 square feet of office space.
2. A bulk storage warehouse located on White Oaks Sideroad in London, comprising 60,000 square feet.
3. Warehouse buildings located in the central areas of London (27,000 square feet), Sarnia (6,000 square feet), and Kitchener (3,000 square feet), each of which is dedicated to the distribution of electrical construction material.

As with most business, revolutionary changes have occurred in hardware merchandising over the last 75 years. If in the early 1900s the wholesaler was dominant, it was because the manufacturer depended completely on his aggressiveness, ingenuity and financial strength to get his goods to the right market. But by 1945, the manufacturer was beginning to take the initiative, as he concentrated his vastly expanded production capacity on consumer goods. The consumer responded well, pressing for more products, and better availability of products, spurred on by highly persuasive advertising. Pressured by unaccustomed volumes and demands, the traditional system of supply faltered. Innovative forms of retailing appeared overnight. The traditional distributor was faced with a dilemma.

A new type of wholesaler claimed the position of control in such a market system, by providing dealer customers with the service and systems they required to cope with their competition. One of the techniques by which this was done, was through the use of franchises, and agreements which embodied many aspects of a franchise. These are the methods that Howden chose in 1964. They continue today to spark growth and profitability. Some indication of growth trends in the Company over the last several decades is shown in the following table:

	Gross Sales
Sales Recorded in 1976	$60,300,000
Annual Average Sales 1970 - 1976	$36,640,000
Annual Average Sales 1960 - 1969	13,874,000
Annual Average Sales 1950 - 1959	7,329,000
Annual Average Sales 1940 - 1949	3,411,000
Annual Average Sales 1930 - 1939	1,466,000

Howden stresses franchises and contracts with all its several classes of retail dealers.

With its Pro Hardware retailers, a formal franchise is executed, bestowing on the dealer benefits of identification as well as purchasing and merchandising privileges and many forms of dealer systems. With its Builders' Supply customers, the contract of supply, while similar, is specialized in other ways to fit the requirements of such dealers. Sporting Goods retailers enjoy like contractual benefits.

To make an integrated merchandising system effective, several important operating components are necessary in addition to the franchise factor. At the supply level the distributor relationship with manufacturers must be such that quality merchandise in proper volumes and at the most competitive prices is always available. The organizations Howden uses for this purpose are Pro Hardware (Canada) Limited (Procan), Span-Canada Electric Limited (Spancan) and Supreme Sports Limited. Each company groups together the purchasing power of its respective shareholders (all non-competing distributors)



and thus is able to create the best contractual arrangements for supply from manufacturers. There is mutual benefit in this integration since the manufacturer is better able to plan production and less subject to high selling costs.

The arrangement is particularly important for the Company's electrical distribution arm. Its marketing field does not lend itself readily to franchises or customer contracts. But it does benefit substantially from integration with suppliers through Spancan.

Another major auxilliary needed for good franchise effect is the organization that the distributor must set up to provide advertising, merchandising, store engineering, and retail data processing systems to its dealers. Without such services, the dealer becomes a lone operator, deprived of the important skills and knowledge he needs to cope with his formidable competition. Howden uses a separate Division for these services. The gross income it earns is consistent with the increase in sales to retailers. It is not however intended to be a major profit centre, but to support our dealers and to make our total program workable.

AND...WHAT IS HAPPENING TO HARDWARE DEALER SALES AND MARKETS?

Certainly sales to all our dealers were excellent during the first three quarters of the year. Last quarter results however, dropped off projection. As a result our net increase for the year of 15% was off budget by 5%. Gross margins declined throughout the year.

Several influences were at work. A tightening in the competitive merchandise pricing environment affected both sales and gross margin. During the year, particularly in the last quarter, the consumer trend was to emphasis on "sale" items, in preference to standard shelf merchandise. This appears to be in keeping with consumer attitudes related to almost all commodities, and could well be expected to change only as do the economic times.

Use of promotional "sales" has always been a strong plank in the Pro retail hardware dealer's platform. These programs are created by special staff working under Procan. All aspects of the promotion are put together by this group – from choosing the products, to creating the copy, to producing the advertising material, whether it be catalogues, flyers, advertising kits, radio or television. The distributor – Howden – plays its role by arranging that each of its franchisees is properly informed, then outfitted with advertising promotional materials, then supplied with the right volume of the items being promoted. Creating and servicing such promotional sales calls for much in the way of dynamics. Normally there are 7 such sales each year, which go under such descriptive headings as "1¢ Sale", "Red Tag Sale", "The Spring Catalogue", "Summer Sale", "Christmas Sale", and others.



Promotional sales however do not constitute the bedrock of a franchisee's enterprise. To succeed he must maintain a basic stock plan – a balanced inventory of merchandise comprised of those fundamental items which consumers need at regular intervals, which turn rapidly, and profitably, and which give maximum sales return on the square footage of selling space available.

The Pro franchisee, an independent business man, operates on his own capital, relies on his own ingenuity and administrative powers. Howden's role is to supply him not only with merchandise, but with systems, and instruction so that he can operate his store in a professional manner. Hence the basic stock plans, automatic ordering devices, inventory control techniques, gross margin guidance, retail accounting systems, and many other devices that issue from Howden programs.

The market thus created and fostered by our 290 franchisees has shown consistently high annual increases since 1970, even allowing for inflation.

But what of the future?

In the beginning, the Pro system found its basis of strength in the small cities and towns. Now incursions are being made into densely populated urban areas. Outlets which function well in such environments are necessarily high volume installations. Their costs are also necessarily high, living as they do side by side with major retailers such as Simpsons, Eatons, Canadian Tire and others. They have however at least three specific advantages, the first being specialized product knowledge, which many of their competitors do not have. Then they have competitive pricing. And finally they have merchandising expertise at their beck and call from Howden sources. We look for significant advances in this market in 1977 and 1978.

There are other assurances of sales growth, leaving aside the normal expectancy of keeping pace with population advances, especially in Ontario. Upgrading of existing dealer outlets is always a powerful stimulus to new sales. Relentlessly the unprogressive dealer fades from the scene, to be replaced, often in a more favourable location by a vigorous newcomer. Better financed, better managed, better able to support a programmed system of distribution, and unfettered by space restrictions, the new dealer can grow and expand with his surrounding community.

The Division is cognizant indeed of the sluggishness of our economy in this spring of 1977 and its implications for the months to follow. Nonetheless, by reason of its aggressive approach to the development of its Pro franchise system in urban Ontario, the Maritimes and the Atlantic Provinces, the Division has set an increase of 10% for its target in 1977.

AND A LOOK AT BUILDING SUPPLY DEALER SALES AND MARKETS

The Watford dealer who sold coal, coal oil, cord wood and other fuels at the turn of the century is the man who today might be contractually allied to Howden as a building supply dealer customer. Over the years, many coal and fuel dealers with their extensive yard space, added lumber and building supplies. The post-war boom gave them great impetus, and they gradually expanded their operations to include the sale of consumer "do-it-yourself" merchandise. The growth of this specific market, coupled with the decline of the small home builder, had made it increasingly a very important segment of the new, modern home improvement dealer's business offer.

As a supplier to such dealers, Howden's Building Supply Division again enjoyed a record year, increasing its sales by 44%. There was however a tendency towards lowered margins due to highly competitive pricing.

The product lines for retail customers of the Division lean toward tools, power tools, electrical, plumbing, decorative items and construction materials, and all mechanical needs that the do-it-yourself market implies. These products provide a natural complement to sales of building materials.

Our building supply dealer has certain similarities to our Pro Hardware dealer. He too is an independent business man, reliant on his own resources, responsible for his own achievements, and sensitive to the tremendous competition he faces as an independent merchant. As a consequence, in almost all cases, he allies himself to a formal organization of his fellow building supply dealers. From that organization he receives national identity, purchasing privileges for lumber products – his main stock in trade – and the pooling of merchandising expertise.

In its turn and from its vantage point, our Building Supply Division is then able to service the remaining and growing sector of his business – those consumer hardware and do-it-yourself items which go hand in hand with the consumer's need for wood and related products.

The techniques the Division uses are not dissimilar from its Procan counterpart: a model stock program to provide guidance in establishing a needed inventory pattern; inventory control techniques; advertising programs, store engineering services and other programs more specifically directed to the builders' supply market.

The Division has achieved very striking sales growth in the past three years. Its 700 dealers cover all of Ontario, some portions of Quebec, the Maritimes and Newfoundland. And there is still room for growth in all of those areas.

The challenge for 1977 is the development of dealers in British Columbia and Alberta. Currently 8 major yards of the West Fraser Building Supply Group are being serviced – all new in 1977. In addition, 20 yards identified with major Canadian lumber groups receive regular shipments.

All of these accounts are serviced out of the main facility in London. The logistics as to transportation are complex, and in 1976 were costly. With the present configuration of dealers, more realistic freight costs are at hand. As volume increases through 1977 freight costs will fall within a controlled relationship with sales volumes.

DISTRIBUTION IN THE ELECTRICAL CONSTRUCTION MATERIAL MARKET

In the Thirties and Forties, the finishing stages of the electrification of Western Ontario were taking place. The war years intervened of course, and in so doing precipitated a tremendous jump forward during the late Forties and early Fifties.

As if the expected post-war boom in all industry was not enough, there was also a huge Province-wide program to convert all electrical equipment from 25 to 60 cycles. It alone encouraged great expansion in many types of electrical equipment which had enjoyed only limited use before. New products began to appear. As industry responded to continuing consumer pressures, electrical construction materials were in huge demand, accompanied on occasion by great shortages. The demand never stopped at any level. No sooner were 30 amp. residential services accepted and installed, than the requirement became 60, and today is no less than 100. Each ten years the consumption of electric power in Ontario doubles, suggesting an annual rate of about 7% increase.

Numerous distributors found this vigorous market most attractive, and set up shop throughout Ontario – and Canada as well – in the years 1945 to 1950. Howden formed its Electrical Supply Division in 1949. Its function was and is to serve the electrical construction trade, and industrial users. It is interesting that the trend of hardware distribution is towards centralization with supply networks covering a



IN THE GUN SHOP
On the right David Hartford Howden, on the left John Valentine Givins, to his left - an inquiring hunter and Lyle Johnston.

broad territorial range, while electrical distribution tends to adopt a more retail profile, with branch operations supplying a smaller trading area.

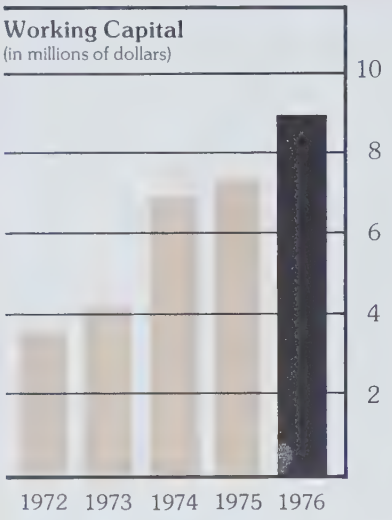
The Division grew rapidly. Throughout the Sixties it achieved an annual 15% growth rate, on profitable terms. Currently it provides somewhat less than 15% of the Company's sales volume.

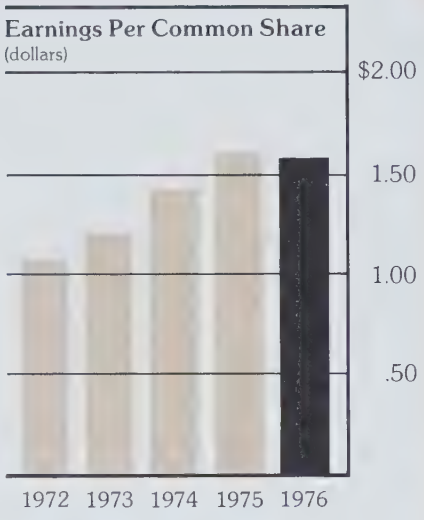
As experienced by many similar distributors, 1976 was not a good year for either sales expansion or profitable operation. Residential building and industrial construction remained in the doldrums. Sales were made under extreme competitive pressure. As a result, while its '76 sales were up 8%, gross margins were badly hit, and the Division developed only marginal profits for the year.

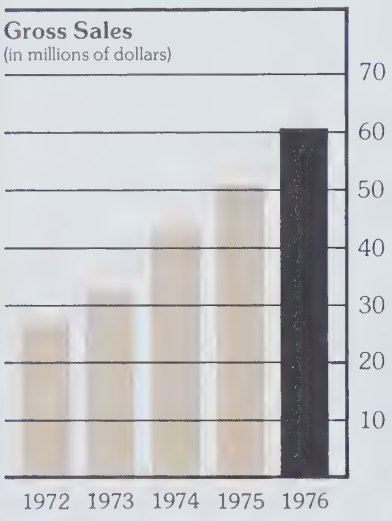
The Division is a member of Span-Canada Electric Limited. This Company is a corporate wholesaler founded in 1965 by Howden. It operates in a manner similar to Pro Hardware (Canada) Limited, with its 17 shareholder members covering geographically the complete Canadian market. Economies in purchasing and marketing research have been of exceptional value over past years. Spancan gives the independent distributor, such as Howden, the purchasing cost base to compete with the giants, G.E., Nedco, Westinghouse, and others, each in their respective trading areas.

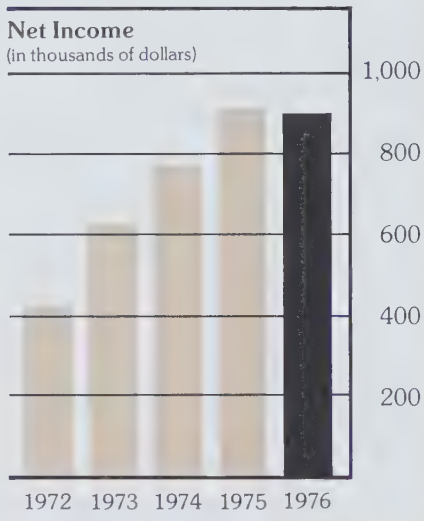
During 1976 our warehousing operations were streamlined. In the face of prevailing cost structures, the marketing function must now be streamlined to create more favourable achievement of gross margin. Full recovery in this Division awaits the return of industrial growth, which in turn depends so much on the restoration of business confidence.

FINANCIAL REVIEW









IN 1976 consolidated gross operating revenue of the Company increased by 18% to $60,300,000. The new record was achieved despite disappointing last quarter sales of seasonal merchandise, and continuing softness in the electrical construction market.

Net income after taxes was $902,782 or $1.59 per common share, compared with $918,958 or $1.62 per common share in 1975.

Inventories increased substantially at year-end, reflecting the requirements of an expanding business, and in particular the anticipated development of significant markets in the Western Provinces during 1977. Also, depressed fourth quarter sales left in their wake inventory surplus of approximately $750,000. Investment in accounts receivable responded well at year-end, dropping by over $500,000 from the year previous, and this in the face of higher sales.

Capital expenditures during the year of $254,000 were directed principally towards the maintenance of warehouse and office changes, equipment required for a new case goods storage area on the White Oaks Sideroad and the support of the Company's automobile and truck fleet. The White Oaks facility, located about one half mile from the Southdale Road location comprises 1.2 million cubic feet. It became fully operative in December, performing the role of a reserve bulk warehouse and a promotional marshalling centre.

The Company's working capital at year-end was improved by $1,578,000 or 21%. Retained earnings accounted for $710,000 of the increase. The balance was generated through sales of a $4,000,000 debenture to a major lending institution. The purpose of the refinancing was to improve the Company's liquidity, and at the same time provide a funding base for continued expansion.

The debenture loan matures in 1984. The interest rate will have a favourable impact on the Company's total borrowing. Short term borrowing needs continue to be well satisfied through the services of the Bank of Montreal.

Dividends of $165,000 were paid to the Company's common shareholders and $27,886 to preferred. During the year the annual dividend rate on the common was raised to 30¢ per share from 25¢. Payments under the Employees' Profit Sharing Plan amount to 7¢ per share, unchanged from last year.

Shareholder Equity now stands at $6,338,785, an increase of $756,646 from 1975. Book value of each common share at December 31st was $10.45 compared to $9.16 a year earlier. Common shares traded during the year were 41,900, with a high of $9 3/4 and a low of $7 3/8.

While sales reached record levels, return on equity dropped from 19% to 16%. Profit margin at 1.59% of sales was down by .32%. Asset turnover (monthly average) was up slightly (2.93 to 3.17). Financial leverage (monthly average) dropped from 3.4 to 3.2.

Year	Net Profit Margin		Asset Turnover		Financial Leverage		Return on Net Worth
1975	1.91	×	2.93	×	3.40	=	19.07%
1976	1.59	×	3.17	×	3.20	=	16.13%

Pressure from the declining ratio of profits to sales is the main reason for the reduction in return on net worth. As referred to in the President's Report to the shareholders, we experienced depressed sales and gross margins, particularly in the fourth quarter, extensive costs of getting the White Oaks installation into production and high initial costs of opening up markets in Western Canada. The last included unusual expenses related to the early stages of a long distance freight program.

These higher cost levels, some being of a one time nature, somewhat lower gross margins, and costly interest charges all interacted to produce a less favourable ratio of operating costs to sales.

The Company's effective tax rate reduced from 47% in 1975 to 44% in 1976. This reduction recognizes the lowering of the basic tax rate, the removal of the 10% surcharge initiated in 1974, and the utilization of a tax loss carry forward in one of the Company's subsidiaries.

D. H. Howden & Co. Limited and Subsidiary Companies
(Incorporated under the Business Corporations Act – Ontario)

Consolidated Balance Sheet as at December 31

Assets	**1976**	1975
Current		
Cash	**$ 138,961**	$ 190,259
Accounts receivable	**7,241,987**	7,789,567
Inventories	**7,919,376**	6,164,665
Prepaid expense	**170,146**	109,799
Income taxes recoverable	**68,863**	—
	15,539,333	14,254,290
Equipment and leasehold improvements	**1,181,082**	939,045
Less accumulated depreciation and amortization	**567,206**	473,481
	613,876	465,564
Other		
Cash surrender value of life insurance	**21,533**	20,634
Equity in corporate joint ventures	**148,204**	178,121
Equity in unconsolidated subsidiaries	**5,730**	5,730
Mortgage and debentures receivable	**—**	26,375
	175,467	230,860
	$16,328,676	$14,950,714

On behalf of the Board

Director D.H.M. STEWART

Director N. McBETH

Liabilities	**1976**	1975
Current		
Bank indebtedness (note 2)	**$ —**	$ 800,000
Accounts payable	**5,846,206**	5,421,582
Accrued charges	**205,788**	315,355
Current portion of long-term debt	**530,800**	285,220
Income taxes payable	**—**	53,882
	6,582,794	6,876,039
Long-term debt (note 3)	**3,407,097**	2,492,536
Shareholders' Equity		
Capital stock (note 5)		
5 1/2% cumulative redeemable participating sinking fund first preference shares of $50 par value each		
Authorized and issued		
1976 - 2,921 shares; 1975 - 3,196 shares	**146,050**	159,800
3% non-cumulative redeemable second preference shares of $1 par value each		
Authorized		
1976 - 1,261,000 shares;		
1975 - 1,264,000 shares		
Issued		
1976 - 446,000 shares;		
1975 - 385,500 shares	**446,000**	385,500
Common shares		
Authorized - 1,000,000 shares without par value		
Issued		
550,000 shares	**621,000**	621,000
Retained earnings	**5,125,735**	4,415,839
	6,338,785	5,582,139
	$16,328,676	$14,950,714

Auditors' Report

The Shareholders,
D.H. Howden & Co. Limited.

We have examined the consolidated balance sheet of D. H. Howden & Co. Limited as at December 31, 1976 and the consolidated statements of income, retained earnings and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the company as at December 31, 1976 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

TOUCHE ROSS & CO.
Chartered Accountants.
LONDON, Ontario,
February 22, 1977

D. H. Howden & Co. Limited and Subsidiary Companies

Consolidated Statement of Income

For the Year Ended December 31

	1976	1975
Gross sales	**$60,276,244**	$51,028,667
Less sales tax	**3,631,700**	3,028,315
	56,644,544	48,000,352
Cost of sales and operating expenses other than items noted below	**54,296,645**	45,645,878
Interest (note 6)	**696,813**	526,138
Depreciation and amortization	**105,654**	93,192
Operating profit	**1,545,432**	1,735,144
Share of net income of corporate joint ventures	**37,350**	8,314
Income before income taxes	**1,582,782**	1,743,458
Income taxes	**680,000**	824,500
Net income for the year	**$ 902,782**	$ 918,958
Earnings per common share	**$1.59**	$1.62

D. H. Howden & Co. Limited and Subsidiary Companies

Consolidated Statement of Retained Earnings

For The Year Ended December 31

	1976	1975
Retained earnings, beginning of year	**$ 4,415,839**	$ 3,662,412
Net income for the year	**902,782**	918,958
	5,318,621	4,581,370
Dividends		
First preference shares	**14,536**	16,466
Second preference shares	**13,350**	11,565
Common shares	**165,000**	137,500
Retained earnings, end of year	**$ 5,125,735**	$ 4,415,839

D. H. Howden & Co. Limited and Subsidiary Companies

Consolidated Statement of Changes in Financial Position

For The Year Ended December 31

Source of working capital	**1976**	1975
Funds provided from operations		
Net income for the year	**$ 902,782**	$ 918,958
Non-fund items		
Depreciation and amortization	**105,654**	93,192
Deferred income taxes	**—**	4,500
Profit on disposal of equipment and leasehold improvements	**(2,394)**	(5,696)
Share of net income of corporate joint ventures	**(37,350)**	(8,314)
	968,692	1,002,640
Disposal of equipment and leasehold improvements	**2,600**	18,531
Reduction of investment in corporate joint venture	**67,267**	57,400
Reduction of mortgage and debenture receivable	**26,375**	6,576
Long-term debt	**1,445,377**	—
Second preference shares issued	**63,500**	45,500
	2,573,811	1,130,647
Application of working capital		
Equipment and leasehold improvements	**254,172**	216,141
Cash surrender value of insurance	**899**	819
Investment in corporate joint venture	**—**	300
Long-term debt	**530,816**	292,664
Reduction of first preference shares	**13,750**	18,950
Redemption of second preference shares	**3,000**	17,000
Dividends	**192,886**	165,531
	995,523	711,405
Increase in working capital	**$ 1,578,288**	$ 419,242

D. H. Howden & Co. Limited and Subsidiary Companies

Notes to Consolidated Financial Statements

For The Year Ended December 31, 1976

1. Significant Accounting Policies

Principles of Consolidation

The consolidated financial statements include the accounts of the company and its wholly-owned subsidiaries, Howden-Howland Limited, Cowan Hardware (1968) Limited and D.H. Howden Stores (Central) Limited.

The equity of D.H. Howden & Co. Limited in unconsolidated subsidiaries consists of the company's investment in Pro Hardware (Canada) Limited and in Span-Canada Electric Limited. Although these two companies are technically subsidiaries of D.H. Howden & Co. Limited through ownership of voting control, in substance they represent corporate joint ventures on the part of a number of non-competing wholesalers who participate in an integrated merchandising programme and volume purchasing. It was considered inappropriate to consolidate the assets and liabilities of these companies since they consist primarily of amounts due from unrelated companies to these subsidiaries on their behalf. All the expenses of these companies and volume discounts derived from their operations are apportioned to participating member companies. The share of D.H. Howden & Co. Limited in these expenses and volume discounts is reflected in the accompanying financial statements.

Investments in corporate joint ventures, Computer Horizons (Canada) and Supreme Sports Limited, are carried at Howden's share of equity therein and advances to such corporations. The company's share of their earnings is included in consolidated net income.

Inventories

Inventories consist of finished goods and are valued at the lower of cost and net realizable value.

Equipment and leasehold improvements

Equipment and leasehold improvements are recorded at cost and depreciated or amortized over their estimated useful lives. Equipment is depreciated using the declining balance method of rates of 20% and 30% and leasehold improvements are amortized using the straight-line method over the term of the lease.

2. Bank Indebtedness

Bank indebtedness is secured by an assignment of accounts receivable.

3. Long-term Debt

	1976	1975
D.H. Howden & Co. Limited		
Bank Loans (Note 4)		
Demand loan secured by accounts receivable	**$1,400,000**	$ —
Term loan, payable $100,000 quarterly with interest 1½% above the prime bank rate and maturing May 15, 1981	**1,800,000**	2,000,000
	3,200,000	2,000,000
8% Mortgage, payable $445 monthly with interest and maturing September 30, 1990	**45,377**	—
6% Secured sinking fund debentures maturing May 1, 1989	**692,520**	760,425
Cowan Hardware (1968) Limited		
8% Mortgage matured October 1, 1976	**—**	17,331
	3,937,897	2,777,756
Less portion due within one year	**530,800**	285,220
	$3,407,097	$2,492,536

The bank term loan and the sinking fund debentures are secured by a floating charge on all company assets. The debentures are subordinate to the bank term loan.

The annual sinking fund provision is comprised of 10% of the company's unconsolidated net income exclusive of extraordinary items. The provision for 1977 is $62,516 (1976 - $67,889).

4. Subsequent Event

Subsequent to the year end, the company issued a $4,000,000 fixed and floating charge debenture, payable $285,714 semi-annually commencing August 1, 1977 and maturing February 1, 1984. The interest rate on the above note will change from time to time in relation to the lender's cost of borrowing. The rate at February 1, 1977 was 9⅝%. Of the total proceeds, $3,200,000 was applied to payment of the bank loans and the balance of $800,000 was used to increase the working capital of the company in 1977.

5. Capital Stock

First preference shares

The provisions relating to the payments of dividends confer upon the holders of first preference shares a right to participate in dividends on an equal basis with the common shareholders up to a maximum of $2 per share, after a dividend of $.06 has been declared on each common share in any calendar year.

The shares are redeemable, at the option of the company upon thirty days notice, at a premium of $1.50 plus any unpaid cumulative dividends.

Under the sinking fund provisions attaching to the shares, 275 shares were purchased for cancellation during the year at the cost of $12,905.

Second preference shares

During the year 63,500 second preference shares were issued for cash and 3,000 shares were redeemed at par value.

6. Interest on Long-term Debt

Interest on long-term debt amounted to $277,693 in 1976 (1975 - $271,784).

7. Lease Commitments

The company has entered into lease agreements with varying expiry dates to November 30, 2000 for certain buildings and equipment. The annual lease payments required for the next five years are as follows:

Year ending December 31, 1977	$ 454,000
1978	443,000
1979	428,000
1980	374,000
1981	332,000
	$2,031,000

8. Remuneration of Directors and Senior Officers

The aggregate direct remuneration for the year of the directors and semior officers amounted to $331,393 of which $294,593 was paid by the company and its consolidated subsidiaries and $36,800 was paid by unconsolidated subsidiaries.

9. Contingent Liabilities

The company is contingently liable in the amount of $246,000 as follows:

Guarantee of trade paper	$194,000
Guarantee of corporate joint venture bank indebtedness	52,000
	$246,000

10. Anti-Inflation Legislation

Because the company is listed on the Toronto Stock Exchange total annual dividends are restricted under the Anti-inflation Legislation to a maximum of $229,740 in the twelve month period ending October 13, 1977. In the period October 14, 1976 to December 31, 1976 the company declared and paid dividends on second preference and common shares totalling $100,038. The restriction that may apply to dividend payments subsequent to October 13, 1977 has not yet been announced by the Government.

11. Comparative Figures

Certain 1975 comparative figures have been reclassified to conform to the presentation adopted for 1976.

FIVE YEAR REVIEW

	1976	1975	1974	1973	1972
Operating Results					
Gross Sales	**$60,276,244**	$51,028,667	$42,766,017	$32,476,731	$27,794,722
Income before income taxes and extraordinary item	**1,582,782**	1,743,458	1,644,495	1,296,869	875,375
Income taxes	**680,000**	824,500	862,500	670,000	444,000
Income before extraordinary item	**902,782**	918,958	781,995	626,869	431,375
Extraordinary item	**—**	—	—	10,000	134,824
Net Income	**902,782**	918,958	781,995	636,869	566,199
Retained earnings	**5,125,735**	4,415,839	3,662,412	3,013,910	2,397,394
Financial Position					
Accounts receivable	**7,241,987**	7,789,567	6,290,762	5,182,223	4,940,433
Inventories	**7,919,376**	6,164,665	5,949,297	3,780,499	3,331,779
Total current liabilities	**6,582,794**	6,876,039	5,520,091	4,995,634	4,662,107
Working capital	**8,956,939**	7,378,251	6,959,009	4,142,126	3,737,735
Long-term debt	**3,407,097**	2,492,536	2,785,200	875,348	991,109
Shareholders' equity	**6,338,785**	5,582,139	4,819,162	3,812,560	3,204,894
Return on Net Worth *(January 1)	**16.13%**	19.07%	20.51%	19.89%	16.22%
Per Common Share					
Earnings before extraordinary item	**1.59**	1.62	1.44	1.21	0.82
Net earnings	**1.59**	1.62	1.44	1.23	1.09
Shareholders' equity	**10.45**	9.16	7.79	6.61	5.38

*Before extraordinary gain



DIRECTORS & OFFICERS

Directors

JOHN W. ADAMS, F.C.A.
Executive Vice President, Treasurer and Director, Emco Limited
Director, Sifton Properties Limited

T. BRAYL COPP
President, Copp Builders' Supply Company Limited

JOHN B. CRONYN
Corporate Director
John Labatt Limited

JOHN D. HARRISON, M.B.E., Q.C.
Partner, Harrison, Elwood
Barristers and Solicitors

DONALD R. HUGHES
President, Span-Canada Electric Limited

NORMAN McBETH
Vice President-Finance, and Secretary Treasurer

DAVID H. M. STEWART
Chairman
President, Pro Hardware (Canada) Limited

JOSEPH H. UNGER
Retired; Formerly President, Metropolitan Stores of Canada Limited

Annual Meeting

The Annual Meeting of the Shareholders of the Company will be held in the Victoria Room, Holiday Inn, City Centre Tower, 300 King Street, London, Ontario, on Friday, the 27th day of May 1977, at the hour of 11:30 a.m.

Head Office

635 Southdale Road
London, Ontario

Associated Company

COMPUTER HORIZONS (CANADA) LIMITED
President - S. R. Millar

Officers

D. H. M. STEWART
President and Chairman of the Board

N. McBETH
Vice President-Finance, and Secretary Treasurer

K. G. ALLASTER, C.A.
Vice President-Controller

W. J. TARVIT
Vice President of Marketing-Hardware Division

F. P. FORAN
Vice President of Marketing-Building Supply Division

C. W. K. LEROY
Vice President of Marketing-Electrical Supply Division

R. C. McKERLIE
Vice President-Merchandising

M. C. HUMPHREY
Vice President-Distribution

M. C. TUCKER
Vice-President, Corporate Planning.

Auditors

TOUCHE ROSS & CO.

Listing of Common Stock

TORONTO STOCK EXCHANGE

General Counsel

HARRISON, ELWOOD,
BARRISTERS AND SOLICITORS

Transfer Agents and Registrars

CANADA TRUST CO.
(Common and Second Preference Shares)
Toronto, Montreal, London, Winnipeg, Calgary, Vancouver

ROYAL TRUST CO. — TORONTO
(First Preference Shares)


HOWDEN